

## Blue Ribbon Commission on Tax Reform- December 6, 2012

### Proposal # 30: Application of sales tax to pre-written computer software made available for access without a download

- Kentucky currently taxes prewritten computer software 1) purchased off the shelf in the store, 2) loaded by the seller on the customer's computer with no physical disk left with the customer and 3) downloaded online to the customer's computer. This proposal is to clarify that tax applies also to access and use of the equivalent software product where the object of the transaction is to obtain and use the software even though possession of the software is maintained by the seller or a third party.
- Prewritten computer software is included in Kentucky's definition of tangible personal property. Kentucky's 6% sales tax applies to "the retail sale of tangible personal property, ***regardless of the method of delivery.***" Some states with similar language already apply sales tax to charges for remote access to pre-written computer software.
- This proposal will clarify and preserve Kentucky's existing tax base on the retail sale of prewritten computer software in similar fashion to previous action addressing the download of computer software and taxation of digital products in the same manner as their tangible counterparts (House Bill 293 passed in 2003 GA to preserve the base on electronic downloads and House Bill 347 passed in the 2009 GA to update language to address digital property).
- In July 2010, Amazon reported its sales of e-books outsold sales of hardbacks. The company crossed the same threshold with paperbacks in January 2011. According to one forecaster, ebook sales are expected to generate \$9.7 billion worldwide in 2016, more than three times the \$3.2 billion the category is expected to generate this year. Through November of the 2012 holiday shopping season, the top product category of Digital Content & Prescriptions (which includes digital book, music and video downloads) has grown by 25% from last year. Software is now following the same path. The global market for cloud computing will grow from \$41 billion in 2011 to \$240 billion in 2020. By 2015, an estimated 24% of all new business software will be sold under this model of remote access.
- The following states currently tax remote access to computer software: **Indiana**, Massachusetts, Michigan, New York, **Ohio**, Pennsylvania, South Carolina, Texas, Utah, Washington and **West Virginia**.

KRS 139.200 imposes the 6% sales tax on gross receipts from retail sales of tangible personal property (covers software sold through traditional channels) and digital property. The proposed amendment will add charges for the right to access and use prewritten software which is equivalent to that which could be obtained from a retailer and used independently by the end user. Excluded from the charges for the right to access and use prewritten computer software are separately stated data processing and information services.